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§ 1.904(i)-1 Limitation on use of deconsolidation to avoid foreign tax credit limitations.

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§ 1.904-1 Limitation on credit for foreign taxes.

(a) *Per-country limitation*—(1) *General*. In the case of any taxpayer who does not elect the overall limitation under section 904(a)(2), the amount allowable as a credit for income or profits taxes paid or accrued to a foreign country or a possession of the United States is subject to the per-country limitation prescribed in section 904(a)(1). Such limitation provides that the credit for such taxes paid or accrued (including those deemed to have been paid or accrued other than by reason of section 904(d)) to each foreign country or possession of the United States shall not exceed that proportion of the tax against which credit is taken which the taxpayer's taxable income from sources

within such country or possession (but not in excess of the taxpayer's entire taxable income) bears to his entire taxable income for the same taxable year. For special rules regarding the application of the per-country limitation when the taxpayer has derived section 904(f) interest or section 904(f) dividends, see § 1.904-4 or § 1.904-5.

(2) *Illustration of principles*. The operation of the per-country limitation under section 904(a)(1) on the credit for foreign taxes paid or accrued may be illustrated by the following examples:

Example 1. The credit for foreign taxes allowable for 1954 in the case of X, an unmarried citizen of the United States who in 1954 received the income shown below and had three exemptions under section 151, is \$14,904, computed as follows:

Taxable income (computed without deductions for personal exemptions) from sources within the United States	\$50,000
Taxable income (computed without deductions for personal exemptions) from sources within Great Britain	25,000
Total taxable income	75,000
United States income tax (based on taxable income computed with the deductions for personal exemptions)	44,712
British income and profits taxes	18,000
Per-country limitation (25,000/75,000 of \$44,712)	14,904
Credit for British income and profits taxes (total British income and profits taxes, reduced in accordance with the per-country limitation)	14,904

Example 2. Assume the same facts as in example 1, except that the sources of X's income and taxes paid are as shown below. The credit for foreign taxes allowable to X is \$13,442.40, computed as follows:

Taxable income (computed without deductions for personal exemptions) from sources within the United States	\$50,000
Taxable income (computed without deductions for personal exemptions) from sources within Great Britain	15,000
Taxable income (computed without deductions for personal exemptions) from sources within Canada	10,000
Total taxable income	75,000
United States income tax (based on taxable income computed with the deductions for personal exemptions)	44,712
British income and profits taxes	10,800
Per-country limitation on British income and profits taxes (15,000/75,000 of \$44,712)	8,942.40
Credit for British income and profits taxes as limited by per-country limitation	8,942.40
Canadian income and profits taxes	4,500.00
Per-country limitation on Canadian income and profits taxes (10,000/75,000 of \$44,712)	5,961.60
Credit for Canadian income and profits taxes (total Canadian income and profits taxes, since such amount does not exceed the per-country limitation)	4,500.00

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Total amount of credit allowable (sum of credits—\$8,942.40 plus \$4,500) 18,442.40

Example 3. A domestic corporation realized taxable income in 1954 in the amount of \$100,000, consisting of \$50,000 from United States sources and dividends of \$50,000 from a Brazilian corporation, more than 10 percent of whose voting stock it owned. The Brazilian corporation paid income and profits taxes to Brazil on its income and in addition paid a dividend tax for the account of its shareholders on income distributed to them, the latter tax being withheld and paid at the source. The domestic corporation's credit for foreign taxes is \$23,250, computed as follows:

Taxable income from sources within the United States	\$50,000
Taxable income from sources within Brazil	50,000
Total taxable income	100,000
United States income tax	46,500
Dividend tax paid at source to Brazil	19,000
Income and profits taxes deemed under section 902 to have been paid to Brazil, computed as follows:	
Dividends received from Brazilian corporation during 1954	50,000
Income of Brazilian corporation during 1954	200,000
Income and profits taxes paid to Brazil on \$200,000	30,000
Accumulated profits (\$200,000 minus \$30,000)	170,000
Brazilian taxes applicable to accumulated profits distributed:	
50,000/170,000 of 170,000/200,000 of \$30,000	7,500
Total income and profits taxes paid and deemed to have been paid to Brazil	26,500
Per-country limitation (50,000/100,000 of \$46,500)	23,250
Credit for Brazilian income and profits taxes as limited by per-country limitation	23,250

(b) **Overall limitation—(1) General.** In the case of any taxpayer who elects the overall limitation provided by section 904(a)(2), the total credit for taxes paid or accrued (including those deemed to have been paid or accrued other than by reason of section 904(d)) shall not exceed that proportion of the tax against which such credit is taken which the taxpayer's taxable income from sources without the United States (but not in excess of the taxpayer's entire taxable income) bears to his entire taxable income for the same taxable year. For special rules regarding the application of the overall limitation when the taxpayer has derived section 904(f) interest or section 904(f) dividends, see § 1.904-4 or § 1.904-5.

(2) **Illustration of principles.** The operation of the overall limitation under

section 904(a)(2) may be illustrated by the following example:

Example. Corporation X, a domestic corporation, for its taxable year beginning January 1, 1961, elects the overall limitation provided by section 904(a)(2). For taxable year 1961 corporation X has taxable income of \$275,000 of which \$200,000 is from sources without the United States. The United States income tax is \$137,500. During the taxable year corporation X pays or accrues to foreign countries \$105,000 in income and profits taxes, consisting of \$45,000 paid or accrued to foreign country Y and \$60,000 to foreign country Z. The credit for such foreign taxes is limited to \$100,000, i.e., $200,000 \div 275,000 \times \$137,500$. The limitation would be the same whether or not some portion of the \$200,000 of the taxable income from sources without the United States is from sources on the high seas or in a foreign country (other than Y and Z) which imposed no taxes allowable as a credit.

(c) **Special computation of taxable income.** For purposes of computing the limitations under paragraphs (a) and (b) of this section, the taxable income in the case of an individual, estate, or trust shall be computed without any deduction for personal exemptions under section 151 or 642(b).

(d) **Election of overall limitation—(1) In general—(i) Manner of making election.** The initial election under section 904(b) of the overall limitation provided by section 904(a)(2) may be made by the taxpayer for any taxable year beginning after December 31, 1960, without securing the consent of the Commissioner. The taxpayer may, for the first taxable year for which the election is to be made, make such election at any time before the expiration of the period referred to in paragraph (d) of § 1.901-1 for choosing the benefits of section 901 for such taxable year. Having made the initial election, the taxpayer may, within the time prescribed for making such election for such taxable year, revoke such election without the consent of the Commissioner. If such revocation is timely and properly made, the taxpayer may make his initial election of the overall limitation for a later taxable year without the consent of the Commissioner. If, however, the taxpayer makes the initial election for a taxable year and the period prescribed for making such election for such taxable year expires, the taxpayer must continue the election of

the overall limitation for all subsequent taxable years (whether or not foreign taxes were paid or accrued for any such year and notwithstanding that a deduction for foreign taxes under section 164 was claimed for any such year) until revoked with the consent of the Commissioner. See section 904(b)(1). If the election for any taxable year is revoked with the consent of the Commissioner, the taxpayer may not make a new election for such taxable year or for any subsequent taxable year without the consent of the Commissioner. If the election of the overall limitation is revoked for a taxable year, the per-country limitation shall apply to such taxable year and to all taxable years thereafter unless a new election of the overall limitation is made, either with or without the consent of the Commissioner in accordance with this section.

(ii) *Revocation for first taxable year beginning after December 31, 1969.* Notwithstanding subdivision (i) of this subparagraph, if the taxpayer has made an initial election under section 904(b) of the overall limitation for a taxable year beginning before January 1, 1970, and the period prescribed for making such election for such taxable year has expired, or if he has made a new election for such a taxable year with the consent of the Commissioner, he may revoke such election effective with respect to his first taxable year beginning after December 31, 1969, without the consent of the Commissioner. Such revocation may be made within the time prescribed for making an initial election for such first taxable year beginning after December 31, 1969. If such revocation is timely and properly made, the taxpayer may make a new election of the overall limitation for a later taxable year without the consent of the Commissioner. Such new election for a later taxable year may be made at any time before the expiration of the period referred to in paragraph (d) of § 1.901-1 for choosing the benefits of section 901 for such taxable year. The revocation of an election, or the making of a new election, pursuant to this subdivision shall be made in the same manner provided in subparagraph (2) of this paragraph for revoking or making an initial election. This sub-

division applies even though the taxpayer is not required under section 901(e) and § 1.901-3 to reduce the amount of any foreign taxes paid, accrued, or deemed to be paid with respect to foreign mineral income for any taxable year beginning after December 31, 1969.

(2) *Method of making the initial election.* The initial election of the overall limitation under section 904(b) shall be made on Form 1116 in the case of an individual or on Form 1118 in the case of a corporation. The form shall be attached to the appropriate income tax return for the taxable year to which such election applies. Such election may be made, however, only for a taxable year for which the taxpayer chooses to claim a credit under section 901. If the taxpayer revokes the initial election without the consent of the Commissioner, he must file amended Form 1116 or 1118 and amended income tax returns or claims for refund, where applicable, for the taxable years to which the revocation applies. For rules relating to the filing of such forms, see paragraph (a) of § 1.905-2.

(3) *Method of revoking an election and making a new election.* A request to revoke an election of the overall limitation under section 904(b) when such revocation requires the consent of the Commissioner, or to make a new election when such election requires the consent of the Commissioner, shall be in writing and shall be addressed to the Commissioner of Internal Revenue, Washington, D.C. 20224. The request shall include the name and address of the taxpayer and shall be signed by the taxpayer or his duly authorized representative. It must specify the taxable year for which the revocation or new election is to be effective and shall be mailed within 75 days after the close of the first taxable year for which it is desired to make the change. It must be accompanied by a statement specifying the nature of the taxpayer's business, the countries in which the business is carried on, or expected to be carried on, within the taxable year of the requested change, and grounds considered as justifying the requested revocation or new election. The Commissioner may require such other information as may be necessary in order to

determine whether the proposed change will be permitted. Generally, a request for consent to revoke an election or make a new election will be granted if the basic nature of the taxpayer's business changes or if there are changes in conditions in a foreign country which substantially affect the taxpayer's business. For example, a taxpayer who enters substantial operations in a new foreign country or who loses an existing investment due to nationalization, expropriation, or war would be granted consent to revoke an election or make a new election.

(e) *Joint return*—(1) *General*. In the case of a husband and wife making a joint return, the applicable limitation prescribed by section 904(a) on the credit for taxes paid or accrued to foreign countries and possessions of the United States shall be applied with respect to the aggregate taxable income from sources within each such country or possession, or from sources without the United States, as the case may be, and the aggregate taxable income from all sources, of the spouses.

(2) *Electing the overall limitation*. If a husband and wife make a joint return for the current taxable year, but made a separate return for the preceding taxable year and the overall limitation applied for such preceding taxable year to one spouse or to both spouses (whether or not then married), then, unless revoked with the consent of the Commissioner, the overall limitation shall apply for the current taxable year and for subsequent taxable years of both spouses, whether or not they remain married, whether or not joint returns are filed for such subsequent taxable years, and whether or not one of such spouses could have elected the overall limitation for the current taxable year only with the consent of the Commissioner if he had filed a separate return for such year.

[T.D. 6789, 29 FR 19243, Dec. 31, 1964, as amended by T.D. 7294, 38 FR 33080, Nov. 30, 1973; T.D. 7490, 42 FR 30497, June 15, 1977; 42 FR 32536, June 27, 1977]

§ 1.904-2 Carryback and carryover of unused foreign tax.

(a) *Credit for foreign tax carryback or carryover*. A taxpayer who chooses to claim a credit under section 901 for a

taxable year is allowed a credit under that section not only for taxes otherwise allowable as a credit but also for taxes deemed paid or accrued in that year as a result of a carryback or carryover of an unused foreign tax under section 904(d). However, the taxes so deemed paid or accrued shall not be allowed as a deduction under section 164(a). The following paragraphs of this section provide rules for the computation of carryovers and carrybacks under section 904(d). For special rules regarding the application of section 904(d) and this section in the case of taxes paid or accrued with respect to section 904(f) interest see section 904(f) and § 1.904-4. For special rules regarding the application of section 904(d) and this section in the case of taxes paid, accrued, or deemed to be paid with respect to section 904(f) dividends see section 904(f) and § 1.904-5. For special rules regarding these computations in the case of taxes paid, accrued, or deemed to be paid with respect to foreign oil and gas extraction income or foreign oil related income, see section 907 (b), (e), and (f) and the regulations thereunder.

(b) *Years to which carried*—(1) *General*. If the taxpayer chooses the benefits of section 901 for a taxable year beginning after December 31, 1957, any unused foreign tax (as defined in subparagraph (2) of this paragraph) for such year shall, under section 904(d), be carried to the second preceding taxable year, the first preceding taxable year, and the first, second, third, fourth, and fifth succeeding taxable years, in that order and to the extent not absorbed as taxes deemed paid or accrued, under paragraph (c) of this section, in a prior taxable year. The entire unused foreign tax for any taxable year shall first be carried to the earliest of the taxable years to which, under the preceding sentence, such unused foreign tax may be carried. Any portion of such unused foreign tax not deemed paid or accrued under paragraph (c) of this section in such earliest taxable year shall then be carried to the next earliest taxable year to which such unused foreign tax may be carried, and any portion not absorbed in that year shall then be carried to the next earliest year, and so on.